

INTERNAL REVENUE SERVICE
District Director

DEPARTMENT OF THE TREASURY
1100 Commerce St.
Dallas, TX 75242

Person to Contact:

Telephone Number:

Refer Reply to:

Employer Identification Number:

Date: AUG 15 1996

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under section 501(c)(4) of the Internal Revenue Code. The information submitted indicates that you were incorporated on [REDACTED]. The stated purposes in your organizing documents are:

"The primary purpose to which the Corporation shall be devoted is to implement, operate and maintain a group purchasing organization for health services for business entities in the [REDACTED] metropolitan area."

Article I, Section 1.3, of your bylaws, states that you are formed to "contract with healthcare facilities and physicians who provide health care services (Providers) for health care related services for the employees of the members of the Corporation and the Employees' dependents. It is anticipated that the Corporation will enter into agreements (herein referred to as Provider Agreement) with Providers and/or medical groups selected and approved by the Board of Directors. Each Provider and medical group who associates with the Corporation as a Provider shall be required to execute a Provider Agreement."

Article II, Section 2.2, of your bylaws, states, "Membership shall be open to any person, business, entity, or organization that meets the following criteria:

1. Has a place of business in [REDACTED]
2. Pays the annual assessment, or upon Board approval, provides in-kind services.

The Corporation shall have two classes of members: Corporate and Associate, with each class segmented as follows:

1. Corporate: has a principal business objective that does not include consulting on, providing, insuring, or brokering health care services or health insurance.

2. Associate: has a principal business objective that includes consulting on providing, insuring, or brokering health care services or health insurance.

The Board of Directors shall establish the procedures, qualifications and other admission requirements of all additional members and, at their sole discretion, may create additional classes of members.

In response to our inquiry about your activities and operations, you submitted the following:

"The [redacted] represents employers and their employees as a single focal point for direct contracting and group purchasing healthcare services from medical providers and facilities. Unlike many 'managed care systems', the [redacted] performs a 'Value based' purchasing function that benefits the entire [redacted]. First, the [redacted] allows any qualified provider or any employer to join the coalition. Providers agree to submit all patient 'outcomes data' from all of their patients to the [redacted] for quality analysis and review. The data is reviewed and the results are reported to both the purchasers and providers of care. This feedback loop is unique in the health care industry. The data can be used by the providers to analyze and review their healthcare services. Healthcare purchasers use the data to help them determine which hospitals and providers within the 'network' they want to obtain healthcare services from in the future. This data will eventually be utilized to create a quality of care benchmark for the community. This is exactly the type of information that is needed to help [redacted] make intelligent healthcare purchasing decisions. The [redacted] has hired a professional management company to handle the day-to-day operations of the [redacted]. The company is called [redacted], a for-profit professional corporation. They are paid any access fees they collect from the employers to administer and grow the purchasing organization."

"[redacted] activities on behalf of [redacted] include (but are not limited to) solicitation, rate negotiations and contract administration of providers, solicitation of new employer members, meeting with and administering contracts with third party vendors for quality analysis, claims repricing, booklet printing, meetings with employers and providers on administrative issues, quality analysis, board and special interest meetings, and answering provider and employer questions as needed."

"The community value of [redacted] is the fact that the 'value purchasing' method of medical services focuses the providers and purchasers into an ongoing cycle of quality and process improvement that benefits the entire community. The open member policy of the [redacted] allows all interested parties to take advantage of this [redacted], which helps make quality

healthcare available to all on a more cost effective basis. Any fees and revenue derived by the board and members of the [redacted] go directly into administration of the program, there is no dividend or revenues paid to the member organization."

The management company spends [redacted] of its time on the following activities:

- Provider solicitation and negotiation:
- Employer solicitation:
- Administering third party contracts for repricing:
- Administering third party contracts for printing:
- Administering third party contracts for quality analysis:
- Administering third party contracts for credentialing:
- Administering other miscellaneous contracts:
- Meetings with providers:
- Meetings with employers:
- Board and other meetings:
- Answering provider and employer questions:

The governing body of the [redacted], its board of directors, is responsible for overseeing the policy and direction of the [redacted] and is responsible for interfacing with the management company. One hundred percent of the Board time is dedicated to these issues, but the actual quantity of time is minimal.

One hundred percent of all [redacted] revenue is dedicated to the aforementioned activities, including oversight of the quality data analysis."

Your Form 1024 states that your present and future income sources will be from membership service fees, fees for repricing member health claims, physicians credentials and recredentialing service and other miscellaneous fees.

Section 501(c)(4) of the Internal Revenue Code provides exemption for:

"Civic Leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare..."

Section 1.501(c)(4)-1 of the regulations provides, in part, as follows:

"(a)(1) In general. A civic league or organization may be exempt as an organization described in section 501(c)(4) if -

- (i) It is not organized or operated for profit; and
- (ii) It is operated exclusively for the promotion of social welfare."

"(a)(2)(i) An organization is operated exclusively for the promotion of social welfare when it is primarily engaged in promoting, in some way, the common good and general welfare of the people of the

community. An organization embraced within this section is one which is operated primarily for the purpose of bringing about civic betterments and social improvements *** The promotion of social welfare does not include direct or indirect participation or intervention in political campaigns on behalf of or in opposition to any candidate for public office. Nor is an organization operated primarily for the promotion of social welfare if its primary activity is operating a social club for the benefit, pleasure, or recreation of its members, or is carrying on a business with the general public in a manner similar to organizations which are operated for profit.***"

Revenue Ruling 73-349, 1973-2 C.B. 179, holds that an organization formed for the purpose of purchasing groceries for its membership at the lowest possible prices on a cooperative basis is not exempt from tax as a social welfare organization under Section 501(c)(4) of the Code. It receives orders from its members, consolidates them, and purchases the food in quantity. Each member pays for the cost of its food. In addition, each member is assessed an equal monthly service charge by the governing board of trustees for the monthly operating costs of the organization. Membership is open to all individuals in a particular community. The organization is a cooperative enterprise for the economic benefit or convenience of the members.

New York State Association of Real Estate Boards Group Insurance Fund V. Commissioner, 54 T.C. 1325 (1970), defines a small group organized fund to obtain group insurance for its members. The insurance was offered only to a limited class of its members and their employees. Since the fund was organized for the benefit of its members only, the court held it does not qualify under Section 501(c)(4) of the Code.

You are encouraging business employers to use the healthcare products offered by your organization. You state that your products are economically priced. Your products include different plans for participating employers to select. You are directly competing with those of a for profit entity that sells or underwrites healthcare policies. Therefore, your health plans and insurance services constitute a kind of business ordinarily carried on for profit.

Like the organization in Rev. Rul. 73-349, you are operating primarily for the benefit of your members, and any benefit to the community is not sufficient to meet the requirements of the regulations that organizations be operated exclusively for the promotion of social welfare.

We have also considered your involvement in the dissemination of information about the healthcare industry. Though this information is beneficial to the general public, it only comprises a very small amount of your operations.

Accordingly, we conclude that you are not a civic organization as described in Section 501(c)(4) of the Code and that you do not qualify for recognition of exemption from federal income tax. Therefore, you should file federal income tax on Form 1120.

We also conclude that you are not a business league as described in

[REDACTED]

Section 501(c)(6) of the Code, because you your purpose is to supply services enabling your members to secure healthcare products more cheaply than if they had to secure them on an individual basis.

If you do not agree with these conclusions, you may, within 30 days from the date of this letter, file in duplicate a brief of the facts, law, and argument that clearly sets forth your position. If you desire an oral discussion of the issue, please indicate this in your protest. The enclosed Publication 892 gives instructions for filing a protest.

If you do not file a protest with this office within 30 days of the date of this report or letter, this proposed determination will become final.

If you agree with these conclusions or do not wish to file a written protest, please sign and return Form 6018 in the enclosed self-addressed envelope as soon as possible.

If you have any further questions, please contact the person whose name and telephone number are shown at the beginning of this letter.

Sincerely,



Bobby E. Scott
District Director

Enclosures:
Publication 892

cc: [REDACTED]